# Trends Of Polish Enterprises In Risk Management

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## Abstract

The beginnings of the implementation of the concept of risk management in the functioning of enterprises stretches back to the middle of the 20th century. Initially they first and foremost signified insurance protection. Subsequent to this, companies began to perceive that not all risk may be insured against and consequently implemented appropriate actions by controlling the level of risk and its impact on enterprises. At the end of the last century, the idea of a complex risk management developed, thus encompassing all types of threats existing in an enterprise (Wieterska 2011, p.11). The effect of the development of the concept of risk management is the formation of a multitude of scientific concepts relating to risk and the international standards of risk management in organizations. The problems associated with the implementation of the systems of risk management have become the subject matter of multiple research projects and works. In the herein paper, the authors at hand present the idea of risk management in Polish enterprises.

**Keywords:** Risk, uncertainty, process of risk management

## Introduction

The progressing globalization, free flow of goods and the growing awareness of consumers are all leading to the fact whereby enterprises are devoting increasing attention to aspects associated with risk management. In conditions of the intensifying change in the market environment, the level of risk and uncertainty in the process of taking decisions is growing. Risk and the associated phenomena constitute an inseparable element of life that is subject to wide-ranging analysis by a variety of specialists. Risk has ceased to be perceived as a threat, but rather increasingly treated in the category of opportunities.

Risk constitutes an inseparable element of every action or decision taken. Its management involves taking decisions and the realization of actions leading to attaining an acceptable level of risk. This is a constant process that involves the search for the optimal connection of two contrasting categories as follows: the maximization of profitability and the restriction of risk at the cost of reducing the predicted revenues. The process of risk management encompasses the following: planning, manipulating risk, monitoring risk, as well as its evaluation and documentation (Department of Defence…2003, p.7).

This paper has been based on the analysis of literature relating to the problematic issues of risk management. Additionally, it is aimed at the illustration of the essence of risk management in Polish enterprises.

## Risk and uncertainty

The genesis of the word risk is derived from the Italian word risicare, which means the undertaking of action in spite of the fact that its effects are uncertain. In this context, the notion of risk is frequently identified with the notion of uncertainty despite the differences that exist between them. Uncertainty exists when there are no possibilities of a prior evaluation of the future levels of parameters in terms of the actions undertaken, as well as the probability of their occurrence. However, risk occurs when on the basis of the analysis of empirical data from the past or on the basis of simulation, there is the possibility of assessing the result and probability of its occurrence.

The precursor of risk management is deemed to be Alan H. Willett, who defined risk as the objectified uncertainty of the occurrence of a future event by noting that it changes together with the uncertainty and not the degree of probability (Willett 1951, p. 6). In the following years, this aspect was further developed by F. Knight, who claimed that uncertainty and risk are presented as different elements, yet possess a common feature – the lack of absolute certainty (Knight 1921, p.17). Risk is the function of uncertainty and possesses two sides - a positive one and a negative one. The positive side arouses creativity, increased mental effort, whereas the latter is the source of aversion to risk.

Hence, risk may be understood as the possibility of the occurrence of events, both positive and negative, which may have an impact on the realization of the intended goals of the enterprise. It prevails in all types of activities and at each stage.

In accordance with the Australian / New Zealand Standard for Risk Management (AS/NZS4360 2004), risk is defined as the possibility of the occurrence of events that have an impact on the chosen aims. These events may help or hinder the achievement of the stipulated aim. These events are defined by the gauge of effects that they may cause, or the probability of their occurrence (Risk Management…2004, p. 3).

The total elimination of risk is not possible, thus every organization agrees to it in order to, among other reasons, achieve the established goal. Simultaneously, its realization brings financial effects with it whose consequences are borne not only by the people taking the decisions, but also the whole enterprise and even their market environment. The losses that an enterprise is exposed to with relation to the business activity run, while also the losses the environment is exposed to by the enterprise, all determine the scope of the inherent risk (Kuchlewska 2003, p. 40). Thus, it is worth bearing in mind that in order to identify the scope of the defined risk, it is essential to establish the causes of its occurrence, while also assess the probability of the possible damage occurring and foresee the possible aftermath. On the one hand, such actions are to lead to the improvement of the company results, while on the other hand ensure that such conditions for running business activity in order for enterprises not to bear any costs that are greater than intended. Hence, it is essential to pursue the restriction of the risk of running business activity to a maximum extent.

## Process of risk management

At present, all enterprises are exposed to different types of risk to a greater or lesser extent. Enterprises should possess the ability to foresee certain events, the skill of fast reactions in order to avail of the emerging market opportunities, as well as prevent and react to the threats. It is significant that firms can manage risk efficiently, which is inextricably connected with running business.

Risk management is the process of gauging risk, or the evaluation of risk and designing of strategies aimed at achieving an acceptable level of risk. Likewise, risk management may also be defined as the widely understood managerial actions, whose task is to identify and evaluate risk, as well as fight against its causes and impact on the organization (Williams, Smith, Young 2002, p. 57).

The process of risk management involves managing the potential effects that results from the uncertainty of running business activity. Risk should be taken into account in every type and area of activities of enterprises. Particularly employees, as well as lower and higher level managers should understand that risk is not a phenomenon that may be managed sporadically or periodically. Threats constantly emerge and it is necessary to deal with them in a complex and systematic manner. They must be included in the routine process of taking decisions, establishing strategies and effective managerment of enterprises.

The approximate elements that compose the process of risk management in an enterprise are presented below:

1. Definition of aims – this requires coordination of risk management with the principles of the enterprise.
2. Evaluation of risk. This consists of three actions that are inter-connected:

– Identification of risk – the aim of this action is to recognise the types of risk and accumulate information on the issue of threats, factors of risk and the susceptibility of enterprises to the existence of losses,
– Analysis of risk, or the way of perceiving risk. At this stage, the nature of the factors of risk are characterized, what evokes it is defined and the manner of its impact on the existence of losses is analysed,
– Measurement of risk – this signifies the definition of the probability of incurring losses, as well as estimating their value depending on the frequency and intensity of occurrence.

3. Control of risk – this refers to all actions in the sphere of monitoring the frequency and/or scale of risk, among others, techniques, tools, strategies and processes that are all aimed to avoid, prevent and restrict risk. Control of risk also encompasses methods whose aim is to have a better understanding of the actions which have an impact on the potential risk. The effective control thus reduces the susceptibility of an organization to risk (Williams, Smith, Young 2002).
4. Financing risk – this involves providing the means to insure against all the losses incurred, as well as financing other programs aimed at mitigating risk (Kościelniak 2008, pp.63-115).
5. Administering the program. Knowledge of the issue of the functioning of a company is required, as well as the aims and factors of production at their disposal. This encompasses the establishment of the procedures that are applied in everyday operations in the sphere of risk management. Likewise, it is also necessary for the firm to have the procedures of informing the market environment of their efforts on behalf of creating the programs of risk management and the results attained (Mrozik 2015, p. 152).

Contemporary enterprises functioning in conditions of new economics must be able to manage risk. Particular stages of risk management are becoming an integral part of the business activities run, while controlling skills in this sphere is becoming a key factor that determines the success of each enterprise operating in conditions of change in the closer and more distant environment.

Depending on the assessment of the magnitude of risk, the possibilities of exposing the enterprises to risk and the potential period of exposure to risk are distinguishable as the following methods of mitigating risk:

- Avoidance of risk – actions are not implemented whereby excessively high risk is attached;
- Acceptance of risk – conscious increase of risk by the enterprise. In this method, the definition of the period of acceptance in which the enterprise is capable of accepting possible losses as permissible;
- Compensation for risk – preparation of such structures of activities in order for the possible loss to formulate as a result of the realization of singular actions and be able to cover this with the profits achieved from other operations;
- Reduction of risk – implementation of managerial action, whose effect shall be the lower probability of realization of a given risk. Such actions include, among others: the correct selection of business partners, defining the necessary contractual clauses;
- Transfer of risk – transferring risk to another entity.

The most frequent methods of transfer are as follows:

- Transfer of liability for the possible losses incurred. This method is exemplified by insurance, or in the case of contracts – stipulating a special clause excluding one of the parties from liability for possible losses that occurred as a result of the execution of a given contract;
- Transfer of activities creating the potential losses – another entity executes the risky part of activities;
- Hedging – the application of the derivative instruments with the aim of mitigating risk.

Implementation of managerial actions and new solutions require the constant monitoring of risk. If it is established that risk is not minimized, it is necessary to carry out a modification of the chosen strategy in order for the recognised risk to be limited to an acceptable level.

## Risk management in Polish enterprises[1]

The report entitled “Risk and insurance management in firms in Poland” (Zarzadzanie ryzykiem i ubezpieczeniami w firmach w Polsce) [2],

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[1] This chapter has been based on the report entitled “Risk and insurance management in firms in Poland 2013/14”, prepared by Aon Polska, whose division of Aon plc (NYSE:AON) is a leading service provider in the sphere of building the strategy of risk management, brokerage of insurance and reinsurance services, as well as advisory services and outsourcing solutions in the sphere of the management of human capital. If the authors do not refer to any literary position in the footnotes, this signifies that they are referring to the afore-mentioned report.

[2] The research was carried out at the end of 2012 and at the beginning of 2013 on the basis of surveys and face-to -face interviews with respondents.

has been prepared by the company Aon Polska Sp. z o.o. since 2009. The cyclical realization of this report facilitates the comparison of the trends in risk management prevailing in Poland with the best practices in this sphere worldwide as Polish research is based on the global research presented in "Aon Global Risk Management Survey". This research facilitates the observation of the most significant trends and tendencies that characterize the Polish market of risk and insurance management – in this paper, the attention of the authors has been narrowed down to merely risk with the deliberate omission of the issues associated with insurance.

A total of 230 respondents took part in the Polish research project, who in their business practices dealt with issues associated with risk management. In global research, this number amounted to 1,400 who represented companies operating in over 70 countries worldwide.

The main group of participants in the Polish research project constituted professionals dealing with company finances, including members of the board relating to financial management, financial directors, treasurers and chief accountansts. The chairmen of boards and managing directors constituted 13% respondents.

Table1. Respondents to research by Aon in Poland and in the world

| Respondent | Polish edition | | | Global edition | | |
|---|---|---|---|---|---|---|
| | 2013 | 2011 | 2009 | 2013 | 2011 | 2009 |
| CFO / Financial Director / Board Member re. Finance | *21%* | *37%* | *34%* | *13%* | *12%* | *5%* |
| Risk Manager / Manager of Risk Management and/or Insurance / Director of Risk Management and/or Insurance | *14%* | *21%* | *11%* | *33%* | *51%* | *54%* |
| CEO / Chairman of Board / General Director / Managing Director | *13%* | *32%* | *3%* | *8%* | *4%* | *2%* |
| Treasurer / Paymaster / Manager of Settlements | *10%* | *5%* | *3%* | *5%* | *2%* | *6%* |
| Chief Administration Officer / Director of Administration, Chief Accountant | *14%* | *10%* | *37%* | *8%* | *1%* | *1%* |
| Company Secretary/ Director / Head Office Manager | *4%* | *26%* | *4%* | *2%* | *2%* | *1%* |
| COO / Operational Director | *3%* | *N/A* | *5%* | *2%* | *2%* | *1%* |
| Others | *21%* | *N/A* | *4%* | *13%* | *10%* | *14%* |

Source: Zarzadzanie ryzykiem i ubezpieczeniami w firmach w Polsce, Raport Aon Polska 2013/14, p. 13.

Attention should be drawn to the fact that the people occupying the managerial positions directly in the sphere of risk management, namely risk managers, constituted approximately 14% of the respondents participating in the research in Poland. Within the framework of identical research of Aon of a global scale, the participation of risk managers was over twice higher, which may certify to the fact of the relatively low popularization of the profession of a risk manager in Poland.

The aim of this research is to define the key risks that may be encountered by enterprises in the forthcoming years. In the current edition of the research, the economic slowdown has returned to the top of the list of threats, which is also a current risk on a global scale (see Table 2).

Table 2. Key 10 risks indicated in Polish and global editions of research 2009-2013

| No. | Ranking of risk 2013 | | Ranking of risk 2011 | | Ranking of risk 2009 | |
|---|---|---|---|---|---|---|
| | **Polish** | **Global** | **Polish** | **Global** | **Polish** | **Global** |
| 1 | Economic slowdown | Economic slowdown | Fluctuations in currency rates | Economic slowdown | Economic slowdown | Economic slowdown |
| 2 | Growing competition | Changes in legislative / regulatory environment | Growing competition | Changes in legislative / regulatory environment | Fluctuations in currency rates | Changes in legislative / regulatory environment |
| 3 | Cash flows / risk of insolvency | Growing competition | Economic slowdown | Growing competition | Fluctuations in prices of raw materials | Break in activities |
| 4 | Trading partners – trading receivables | Loss of reputation | Fluctuations in prices of raw materials | Loss of reputation | Changes in legislative / regulatory environment | Growing competition |
| 5 | Changes in legislative / regulatory environment | Failure to maintain or attract talented employees | Trading partners – trading receivables | Break in activities | Growing competition | Fluctuations in prices of raw materials |
| 6 | Fluctuations in currency rates | Lack of innovativeness | Changes in legislative / regulatory environment | Lack of innovativeness | Trading partners – trading receivables | Loss of reputation |
| 7 | Fluctuations in prices of raw materials | Break in activities | Break in activities<br>Disruption / break in supply chain | Failure to maintain or attract talented employees | Cash flows / risk of insolvency | Cash flows / risk of insolvency |
| 8 | Technological breakdowns | Fluctuations in prices of raw materials | Technological breakdowns | Fluctuations in prices of raw materials | Loss of data | Disruption / break in supply chain |
| 9 | Employee dishonesty | Cash flows / risk of insolvency | Cash flows / risk of insolvency | Technological breakdowns | Disruption / break in supply chain | Civil liability /claims |
| 10 | Civil liability /claims | Political instability | Loss of reputation<br>Civil liability /claims | Cash flows / risk of insolvency | Loss of reputation | Failure to maintain or attract talented employees |

Source: Zarzadzanie ryzykiem i ubezpieczeniami w firmach w Polsce, Raport Aon Polska 2013/14, p. 33.

Economic slowdown has returned to the top of the list of key risks for the business operations of companies in Poland, while simultaneously equalling the position of the results of global research in which the threat associated with economic slowdown has held first position in the ranking for the last three editions of the research. The hitherto key threats, namely the currency rate risk has slipped to sixth place in the ranking. However, the greatest growth in significance among the first ten threats was registered by the risk of insolvency, which increased from ninth position in the previous research to third position in the current ranking. The new risk, which is to be found in the top ten of the Polish edition of research for the first time is that of employee dishonesty, which occupies ninth position. With relation to the global edition of the research, the new threat in the top ten is that of threats associated with political instability around the world. The relatively underestimated threats by Polish companies with regard to the results of global research are as follows: the risk of losing reputation, which incidentally dropped out of the top ten, the risk of the lack of innovativeness and failure to attract and keep talented employees.

Polish enterprises declare the implementation of a formal plan of action. In fact, Polish firms usually have a plan of action with relation to traditional risk, such as for instance, trade receivables, fluctuations of currency rates, or technological breakdowns. Unfortunately, they are not prepared for threats connected with economic slowdown.

Undoubtedly, economic slowdown leads to the formation of financial loss. With relation to both the Polish edition and the global edition of the research, risk associated with economic slowdown led to the formation of financial losses in the largest group of companies under analysis – 73% in Poland and 67% in the international study. In recent times, the level of financial losses as a result of the realization of key risks in Polish companies have significantly risen. With regard to the risk of economic slowdown in the previous edition of research, this percentage amounted to a mere 31%. A similar case is with the second in line in terms of the risk of growing competition, in which the proportion amounted to 62% and 20% respectively. Polish enterprises incur financial loss far more often as the result of the materialization of key risks. Over half of the firms analysed, admitted that they had incurred losses from such risks due to the fluctuation of the prices of raw materials and currency rates. The specifics of the Polish edition of research is the risk of employee dishonesty – over 1/3 of enterprises incurred financial losses arising from this fact (Table 3).

Table 3. Financial losses due to materialization of risk within the past 12 months in terms of the research results for the Polish and global editions of 2013

| No. | Ranking of risk in Poland 2013 | | Ranking of risk in world 2013 | |
|---|---|---|---|---|
| | **Polish edition** | **Losses in 12 months** | **Global edition** | **Losses in 12 months** |
| 1 | Economic slowdown | 73% | Economic slowdown | 67% |
| 2 | Growing competition | 62% | Changes in legislative / regulatory environment | 54% |
| 3 | Cash flows / risk of insolvency | 56% | Growing competition | 50% |
| 4 | Trading partners – trading receivables | 55% | Loss of reputation | 40% |
| 5 | Changes in legislative / regulatory environment | 52% | Failure to maintain or attract talented employees | 37% |
| 6 | Fluctuations in currency rates | 51% | Lack of innovativeness | 37% |
| 7 | Fluctuations in prices of raw materials | 50% | Break in activities | 36% |
| 8 | Technological breakdowns | 38% | Fluctuations in prices of raw materials | 35% |
| 9 | Employee dishonesty | 35% | Cash flows / risk of insolvency | 34% |
| 10 | Civil liability /claims | 29% | Political risk | 30% |

Source: Zarzadzanie ryzykiem i ubezpieczeniami w firmach w Polsce, Report by Aon Polska 2013/14, p. 37.

In practice, risk management is perceived to be the response to a range of challenges associated with running business activities, such as changes in the economic environment, expectations of stakeholders or the occurrence of events that have a particularly significant impact on the functioning of a given enterprise.

In the research, respondents were asked about the key premises of strengthening risk management that determine the principal directions of the development of this discipline. The most important premise for the strengthening of the process of risk management in Poland is that of economic instability that is indicated by 62% of respondents – which is a result of 16 percentage points higher than that achieved in the previous edition of the research. Economic instability also constitutes the most important premise in terms of investments in risk management among the companies participating in the global edition of the research (47%). Over 1/3 of the participants in the research indicated the requirements of investors in the sphere of transparency and liability with relation to taking decisions as one of the main premises for strengthening the system of risk management. This result is over 10% higher than in the case of the global research. Third place, in terms of the most significant external premises encouraging those in managerial positions to invest in the systems of risk management in Poland was occupied by pressure from clients and trading partners – 33%, which also noted the biggest growth in comparison with the research results of the previous years. In comparison with the results of the global research, such premises as the requirements of regulators, extreme natural events, or political instability are of lesser importance (Table 4).

Table 4. Most significant external premises of strengthening of risk management in terms of the research results for the Polish and global editions of 2013

| **Polish edition 2013** | **Percentage of indications in Polish edition 2013** | **Percentage of indications in global edition 2013** |
|---|---|---|
| Economic instability | 62% | 47% |
| Requirements of investors in the sphere of greater transparency and liability | 34% | 22% |
| Pressure from clients | 33% | 20% |
| Increase in interest from regulators | 22% | 34% |
| Extreme natural events | 10% | 18% |
| Political instability | 6% | 15% |
| Others | 9% | 9% |

Source: Zarzadzanie ryzykiem i ubezpieczeniami w firmach w Polsce, Report by Aon Polska 2013/14, p. 41.

In the vast majority of companies that are not financial institutions, they did not shape the organizational structures dedicated for serving the process of risk management to the same degree as their foreign counterparts. The obligations in the sphere of risk management in such a situation are most frequently deployed in the structures of the management of company finances as the most equipped for the complex accumulation of of cross-sectional information on all the activities within the framework of their competences of the established techniques of managing financial risk or purchasing insurance. In the cases of the existence of a separate department of risk management, it is most frequently positioned in the structures subject to the CFO. Rare cases of an autonomous department are most often the result of the adoption of the model of organization of risk management that is currently dominant and is based on the so-called “three lines of defence”. This model assumes that the particular organizational units manage the risk that prevails there, while the department of risk management coordinates and supervises the process and the internal audit ensure a reasonable degree of certainty in terms of achieving the intended results. In other words, liability for risk and the current identification, evaluation and reactions remain within the framework of the particular linear sections, while the basic elements of the activity of the function of risk management are the designing and coordination of the process, ensuring uniform standards and reporting on risk. Thus, in the afore-mentioned model, even large scale activities or the complexity of the organizational structure do not have a significant impact on the scope of tasks in the sphere of risk management attributed to the coordinating entity.

## Conclusion

Risk management constitutes one of the key elements of managing an enterprise, which significantly influences the business efficiency. Indeed, risk management has taken on great significance in the midst of the global economic crisis that we have been facing over the past decade. Up to this point, the methods and standards of risk management had not been commonplace in Poland. As indicated by the research carried out by Aon Polska in Poland, an increasing level of awareness is being observed among the owners and chairmen of companies with relation to the utilization of the standards of risk management.

Appropriate risk management in business activities, as well as the appropriate formation of ties with the immediate environment are among the fundamental prerequisites for ensuring a stable position on the market and the perspectives of further development in a highly com-petitive market.

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